

February 28, 2020

Research Flash Update

Essential Utilities, Inc.

(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	\$46.34
Target Price (\$US):	\$50.00
Market Cap (\$US millions):	\$10,002
ADTV (US\$ millions):	\$67.5
Price as-of Prior Day Close	
Target Price and Rating are for 12 months.	

Estimates	EPS		Revenue (Net)		P/E
	B&S	Cons.	B&S	Cons.	
2018A	\$1.08	-	\$838.1	-	42.9x
2019A	\$1.00	-	\$889.7	-	46.3x
2020E*	\$1.10	\$1.56	\$1,384	\$1,871	42.2x
2021E	\$1.65	\$1.70	\$1,662	\$2,086	28.0x

FYE 12/30; Revenue in USD millions.

*Assumes 3/16/2020 closing for Peoples acquisition.

Source: Capital IQ, B&S Estimates

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Analyst Day Highlights: 2020 guidance just OK, but M&A, three-year growth targets affirm thesis.

Essential Utilities hosted an analyst day at the NYSE, the company's first high-profile public appearance since receiving key PA regulatory approval for the impending acquisition of Peoples Gas. Major topics included the Peoples transaction (reaffirmation of strategic rationale and progress update), municipal acquisition pipeline, 4Q19 earnings, and forward guidance and growth targets. Overall, we came away reinforced in our favorable view of the fundamental story.

With the critical Pennsylvania regulatory approval now secured, the acquisition of Peoples is set to close on 16 March. The regulatory approval process took longer than expected due to the Goodwin-Tombaugh situation (see prior research), and as a result the first full quarter with Peoples on the P&L will be 2Q20. Still, we continue to view the addition of Peoples, which buttresses Essential's already robust regulatory presence in PA and enhances consolidated rate base growth, as a major strategic differentiator vs. peers.

Essential continues to shine on the municipal deal front not only in absolute terms, but also in terms of moving the needle relative to its size. Notable deals include the purchase of Cheltenham WW for \$50 million and the pending acquisition of DELCORA for \$276 million, which together with several smaller deals provide a material tailwind to customer growth. We expect Essential to remain highly active on municipal M&A, with deals outside PA likely to accelerate.

Essential issued 2020 EPS guidance of \$1.53-\$1.58, although given the later than expected Peoples closing, it is on an "illustrative pro forma adjusted" basis (i.e as if Peoples were in for a full 1Q, which it is not). While this means incoming 2020 consensus of \$1.56 could come down, the run-rate pro forma guidance reflects the sustainable go-forward earnings power of the combined enterprise.

Essential initiated three-year growth targets for EPS (5%-7%) and rate base (6%-7% for Aqua, 8%-10% for Peoples). We see these as highly credible targets that Essential can achieve without sowing the seeds of longer-term problems in terms of regulatory/OCA relations, ratepayer affordability in acquired territories, and long-term customer growth. Importantly, Essential's long-term growth targets do NOT include acquisitions, which represent potential upside.

We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated water utility space with notable catalysts. Our price target of \$50 reflects a forward P/E multiple of 30.5 times, in-line with the current peer group average.

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Disclosure Appendix

Rating and Price Target History:



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The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

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Neutral (Hold)	58%	Neutral (Hold)	21%
Underperform (Sell)	0%	Underperform (Sell)	0%
Not Rated	12%	Not Rated	10%

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